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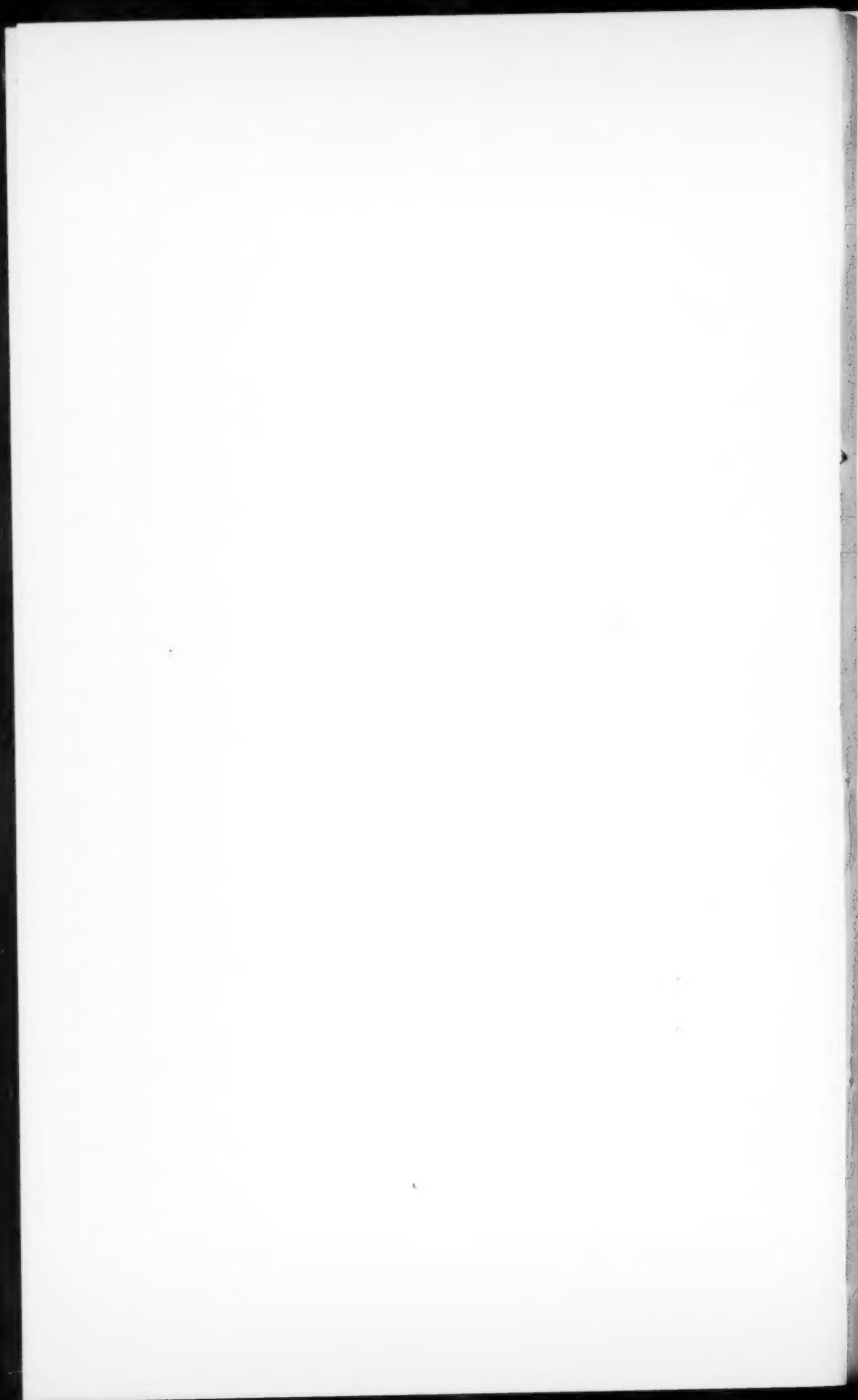


SOME ASPECTS *of the*
CANADIAN BANKING
SYSTEM



SPECIALIZATION
in the PRACTICE *of*
ACCOUNTANCY

OFFICE OF THE SOCIETY
30 BROAD STREET • NEW YORK



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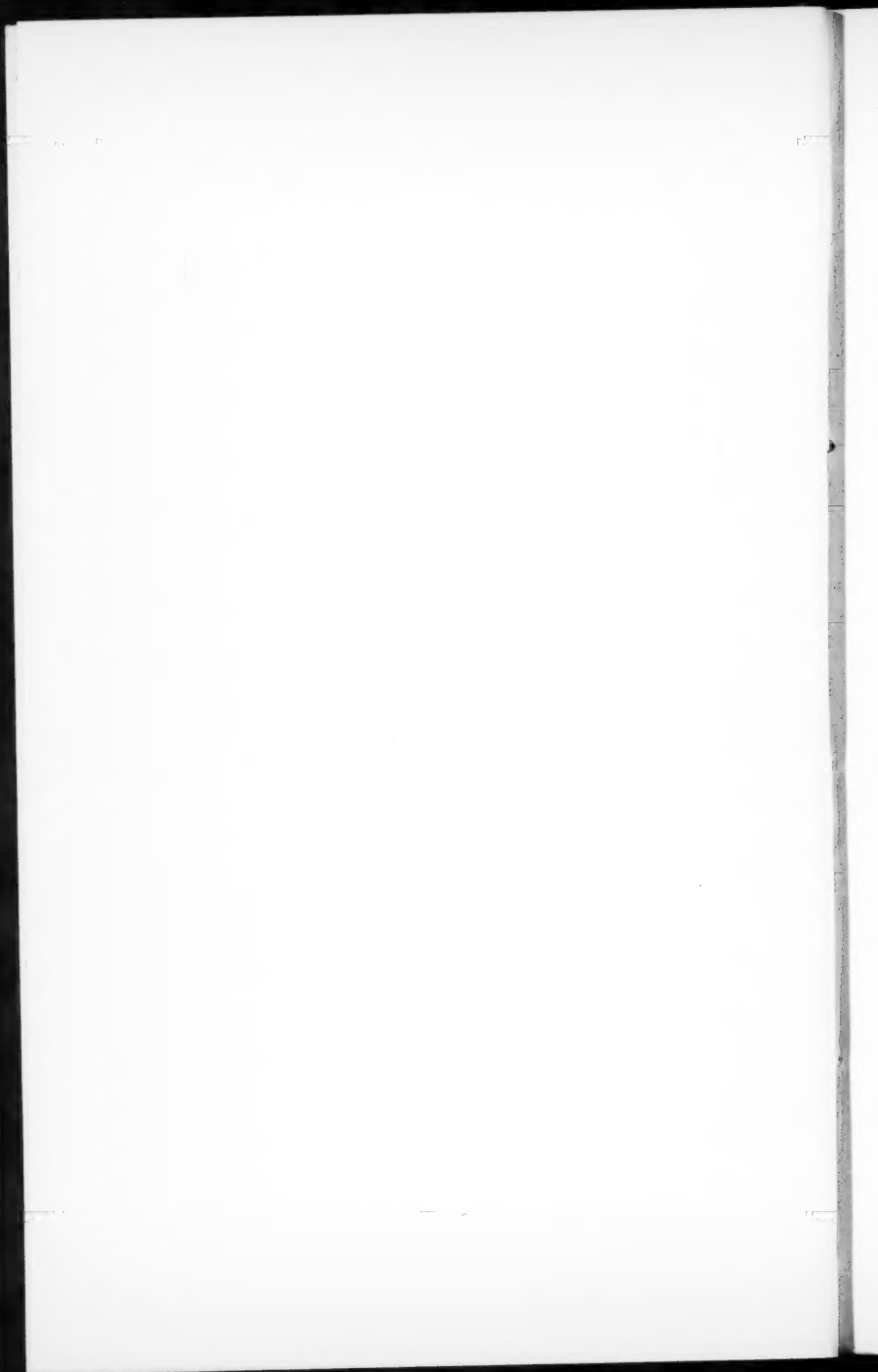
By ANDREW STEWART

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Some Aspects of the Canadian Banking System

By ANDREW STEWART, C. P. A.,
of HASKINS & SELLS

MUCH has been said and written recently regarding the enviable record of Canada, where no bank has suspended since 1923 and only one has closed its doors since 1913. In such circumstances, it is natural that any discussion of this subject would be of particular interest to accountants at the present time.

In Canada, banks operate under a Dominion of Canada charter and banking is thus a federal function. They are regulated by the Canadian Bank Act which it has been the custom to revise every ten years. One section of this Act, which is foreign to any of the banking laws of this country, must be discussed in detail in any address to a society of accountants. I refer to the section entitled, "Shareholders' Audit" under which two auditors are appointed by the shareholders, to whom they are required to report on the condition of the bank at each annual meeting. Before coming to that provision, however, it seems that a general outline, at least, of the Canadian banking system and of the law under which it is regulated is necessary for a proper understanding of the provisions relating to audits.

I do not propose to attempt a complete explanation either of the law or of the methods of operation of Canadian banks, nor do I intend to make any comparison of the Canadian law and system and those of any other country. While some of the more important differences will appear evident from what follows, I shall endeavor to keep strictly within the confines of the title.

The banking of Canada is operated under a branch system as contrasted with the unit system and the banking resources are concentrated in ten chartered institutions.

These ten institutions have an aggregate paid-up capital of \$144,500,000 and rest or reserve funds of \$162,000,000. Two French Canadian banks with a combined capital of \$11,000,000 confine their operations mainly to the province of Quebec. Another bank is a subsidiary of Barclay's Bank of England and has offices only in Montreal and Toronto, so that the seven remaining banks serve practically the whole Dominion. These banks maintain almost four thousand branches located in every city and town throughout Canada and in addition they have about 175 foreign units. It is noteworthy that, in spite of the concentration of the banking business in the hands of a relatively small number of banks, Canada had at the end of 1929 more banking offices on a per capita basis than any other country in the world with the exception of Australia.

Bank Resources Concentrated

During the past twenty years, there has been a marked tendency in Canada, as in most other countries, toward concentration of banking resources. Between 1913 and 1929 twelve Canadian banks became absorbed with other institutions and, as stated, the total number today is only ten.

Each branch has a local manager and usually in each province there is a supervisor who, in turn, reports to the general management and through them to the board of directors. This arrangement, while not impeding speedy decisions regarding smaller loans, provides control over all operations and particularly over the larger ones.

The training of the Canadian banker is favorably regarded all over the world. It is the universal rule that all employees must begin at the bottom, probably as a clerk in a small branch. By slow stages, usually after experience in all departments, he may become accountant, assistant manager and manager. He is then likely to be transferred as manager to different sections of Canada and also to foreign offices where his experience is broadened. He may then become a supervisor and later assistant general manager, general manager, vice-president and president. It is invariably from such a background that the chief executives are de-

veloped. Experience of this sort is, of course, invaluable in directing the management of a national institution.

History of Legislation as to Audits

The first enactment regarding audits of Canadian banks was contained in the Bank Act of June 6, 1913. In it a new section was introduced entitled, "Shareholders' Audits". Since that time this section has been revised only once, in 1923. At this point, I shall explain only the differences between the provisions as to audits as between the 1913 and 1923 Acts. Later on, the provisions regarding audits as enacted in the 1923 Act, which have not been changed since that time, will be dealt with in detail.

In the 1913 Act, the general managers of the banks selected, by ballot, the persons deemed by them to be competent to act as auditors of the banks. They had to select not less than 40, and the only restriction was that no one of them should be a body corporate. Under the 1923 amendment, this power of selection given to the general managers was annulled, and instead the qualifications for bank auditors were that each must be an accountant, who had, for at least six years preceding the date of his appointment, practiced his profession in Canada, and who was a member in good standing of an institute or association of accountants incorporated under the authority of the legislature of any province of Canada. Lists had to be furnished to the Minister of Finance by each such incorporated institute or association of accountants of all their members in good standing, whose names were entitled to be included therein. The Minister of Finance was given power to reduce such lists by selecting names which he considered eligible, but if he did not make such a selection all of the persons on the lists were eligible for appointment.

Under the 1913 Act, the shareholders were given the right of appointment but they were required merely to appoint an auditor or auditors, and if two were appointed they might be partners of the same firm, and they might continue to hold their appointments indefinitely, so long as they were reelected by the shareholders. Under the 1923 Act, it was provided that

two auditors, not members of the same firm, should be appointed, and to insure that they should not continue indefinitely it was also provided that, if the same two persons or members respectively of the same two firms had been appointed for two years in succession, one such person or any member of one such firm should not be again appointed during the period of two years next following the term for which he was last appointed. Thus, while one auditor may hold his appointment indefinitely, the other can hold it for only two years and for the next two years his place must be taken by someone else.

Auditors May Examine Branches

In the 1913 Act, it was specifically provided that if the bank had branches or agencies, it would be sufficient, for all purposes of the audit, if the auditors were allowed access to the returns, reports, and statements, and to such copies of extracts from the books and accounts of any such branch or agency as had been transmitted to the chief office, but the auditors, in their discretion, might visit any branch or agency, for the purpose of examining the books and accounts, cash, securities, documents and vouchers at the branch or agency. This provision was entirely omitted in the 1923 Act, so that the responsibility of the auditor was, if anything, broadened.

There were also certain changes made in the 1923 Act, in the form of the report which the auditor had to make, but they did not make any substantial changes in the intent.

It has been the practice to revise the Canadian Bank Act every ten years. However, an exception was made by certain amendments in 1924, following the failure of the Home Bank in August, 1923. The most important of these was the provision for the appointment of an inspector general of banks, who was given the duty of keeping more closely in touch with the current affairs of the banks than the auditor could possibly do, and who was required to report immediately to the Minister of Finance when he considered that a bank was insolvent.

A further revision of the Bank Act is thus due in 1933, but it is understood that it is likely to be postponed until next

year, so that it may incorporate more fully the experience of the unusual times through which we have been passing.

Organization

No new bank will receive a certificate, permitting it to commence the business of banking, unless the sum of not less than \$500,000 of the capital stock has been bona fide subscribed, and no director shall be eligible to act as such unless he be a bona fide subscriber of stock of the bank for and on his own behalf, so as to become the absolute and sole owner in his individual right of such stock and not as trustee or in the right of another, on which subscription not less than

- (a) three thousand dollars have been *paid up*, when the paid-up capital stock of the bank is one million dollars or less;
- (b) four thousand dollars if over one million and not exceeding three million dollars;
- (c) five thousand dollars if the paid-up capital stock exceeds three million dollars.

The obvious comment on these provisions is that they have assuredly been effective in preventing the creation of a multitude of small banks with insufficient capital, and in preventing the election of irresponsible persons as directors.

All stockholders have a double liability equal to the par value of the shares held by them, in addition to any amount not paid up on such shares, and Section 125 of the Act, which provides for the double liability, must be printed on each page in the stock books upon which subscriptions are recorded, and on every document constituting or authorizing a subscription, so that it may be readily seen by the person recording the subscription.

The directors are required to obtain a bond, guarantee, or other security from all employees, for the due and faithful performance of their duties.

Another interesting provision, in this connection, is the requirement that the notice of the annual general meeting shall state the number of meetings attended by each director.

Dividends

No dividend or bonus shall be declared so as to impair the paid-up capital of the bank. Directors who knowingly and wilfully concur in the declaration of an improper dividend are jointly and severally liable for the amount declared as a debt due by them to the bank.

No division of profits exceeding the rate of 8% per annum shall be made, unless after making the same the bank has a rest or reserve fund of at least 30% of its paid-up capital, after providing all the appropriations necessary for ascertained and estimated losses, and a similar joint and several liability is placed on the directors for violation.

Inspection

In 1924, it was felt that additional safeguards were necessary beyond the provisions for annual audits. Accordingly, provision was made for the safeguarding of banks by an amendment calling for the appointment of an inspector general of banks, whose duties would be "from time to time but not less frequently than once in each calendar year, to make or cause to be made such examination and inquiry into the affairs or business of each bank as he may deem to be necessary or expedient * * * * * for the purpose of satisfying himself that the provisions of this Act having reference to the safety of the creditors and shareholders are being duly observed and that the bank is in sound financial condition, and at the conclusion of such examination and inquiry shall report thereon to the Minister." The inspector has the power to employ such clerical assistance as may be deemed necessary and he is given the powers of a commissioner for the purpose of obtaining evidence under oath.

Whenever the inspector is satisfied that a bank is insolvent, he is required to report fully on the bank's condition to the Minister of Finance, who may, without waiting for the bank to suspend payment, request the Canadian Bankers Association to appoint a curator.

Returns to Minister of Finance

Each bank must transmit to the Minister of Finance within the first twenty-eight days of each month, a return exhibiting

the condition of the bank on the last business day of the month last preceding. The Minister has also power to call for special returns at any time. The form of return, which is appended as Schedule G to the Act, calls for considerable detail, and gives a rather complete picture of the financial position at a given date. It is interesting to note that it calls for a segregation of current loans and non-current loans for which the estimated loss has been provided.

The Act defines current loans by stating that there shall not be included therein any loan in respect of which

- (a) the borrower has not for a period of two years preceding the date of such return, statement or balance sheet, paid the interest thereon at the rate agreed in cash, unassisted by the bank;
- (b) the bank has taken possession of the property or any part of the property covered by any security given by the borrower with the intention of realizing thereon, or has realized or taken any step or proceeding for the purpose of realizing upon any security given by the borrower;
- (c) the bank has commenced an action at law to recover from the borrower the amount of the loan or any part thereof;
- (d) the borrower has made an abandonment of his estate for the benefit of his creditors or any of them; or
- (e) there is other cause, sufficient in the opinion of the manager of the branch of the bank where such loan is domiciled, or in the opinion of any director or officer of the bank who prepares, signs, approves or concurs in such return, statement or balance sheet, for deeming such loan not to be a current loan.

There is an additional provision that any loan falling within the last preceding sub-section may be included in current loans if the directors declare that, after due inquiry, they have approved such loan as a current loan. It may be noted here that the statement, which is presented to the annual meeting of shareholders and which must be certified by the

auditors, calls for a similar segregation as to current and non-current loans.

Annual and Special Statements to Shareholders

I wish to call your attention particularly to the following requirement as to annual statement, because this is the statement which the auditors must certify.

Section 53 reads as follows:

"At every annual general meeting of the shareholders, the outgoing directors shall submit a clear and full statement of the affairs of the bank, exhibiting, on the one part, the liabilities of the bank, and, on the other part, the assets and resources thereof, and the statement shall be signed by the general manager or other principal officer of the bank next in authority in the management of the affairs of the bank at the time at which the statement is signed, and shall be signed on behalf of the board by the president or a vice-president or any other two directors, neither of whom shall be an officer of the bank."

The Act specifies the details of the assets and liabilities which must be disclosed, which may be described as giving a very complete statement of the affairs of the bank. It is also provided that whenever a bank carries on any part of its operations in the name of a corporation controlled by such bank, a statement of such corporation shall also be submitted and the auditors of the bank are to be deemed auditors of such controlled corporation. A copy of the statement and of the profit and loss account, together with a copy of the minutes of the annual general meeting, is required to be sent within four weeks thereafter to each shareholder.

The shareholders are given the right to require additional statements by passing a by-law to that effect at the annual general meeting or at any special general meeting called for the purpose.

To all reports made by directors to shareholders under Section 53, there must be attached the auditors' report which is required to be read before the shareholders at their meetings.

Shareholders' Audit—Qualification of Auditors

I have previously referred to the original provision for shareholders' audits in the Act of 1913.

In the decennial revision of the Act of 1913, which was entitled the Act of 1923, certain important amendments were made with regard to the qualifications of auditors and the method of their election. In particular, the possibility of having two members of the same firm elected as auditors was precluded and in addition the same two auditors were not allowed to continue indefinitely, but one, at least, had to be changed every two years.

Apparently the legislators had in mind the importance of a new viewpoint in auditing, and they possibly also felt that the auditor in such circumstances would be less likely to be a victim of undue influence.

As the law now stands, every bank must be audited by two auditors, not members of the same firm, selected by the shareholders at their annual general meeting. The necessary qualifications are that each one shall be an accountant who has, for at least six years preceding the date of his appointment, practiced his profession in Canada, and who is also a member in good standing of an institute or an association of accountants incorporated under the authority of the legislature of any province of Canada. Each incorporated institute or association of accountants is required to furnish a list of those qualified as above stated. The Minister of Finance may then select from such lists the persons, any one of whom shall be eligible to be appointed auditor, and if he does not make a selection all persons on the lists so furnished are eligible for appointment. This list is then advertised in the Canada Gazette.

An auditor appointed under the Act cannot, either by himself or by his firm, undertake any other employment on behalf or at the instance of such bank during the term of his appointment and whether at the expense of the bank or not. This seems a very salutary provision and was obviously designed to make the auditor as independent as possible.

No person shall be appointed auditor of a bank if he or any member of his firm is a director or officer of such bank.

Shareholders' Audit — Duties of Auditors

The duties of the auditors are clearly described.

First, they are given the right of access to the books and accounts, cash, securities, documents, and vouchers of the bank, and they are entitled to require and receive from the directors and officers, such information and explanation as may be necessary for the prompt performance of their duties. At this point, it is important to note that the Minister of Finance may require the auditors to report to him upon the adequacy of the procedure adopted for the safety of the creditors and shareholders and *as to the sufficiency of their own procedure in auditing the affairs of the bank*, and the Minister may, at his discretion, enlarge or extend the scope of the audit or direct that any other or particular examination be made or procedure established in the particular case, as the public interest may seem to require. This affords the auditor the opportunity of discussing his procedure with the Minister of Finance if at any time he is in doubt as to its adequacy, and a direction from the Minister thereafter would be binding upon his co-auditor and himself.

The Act provides for auditors' reports to directors, from time to time, in addition to their annual report to shareholders, which will be discussed later. This provision is quoted in full:

"It shall be the duty of the auditors to report individually or jointly as to them may seem fit to the general manager and to the directors in writing *any transactions or conditions affecting the well being of the bank which are not satisfactory to them, and which in their opinion require rectification*, and without restricting the generality of this requirement they shall report specifically to the general manager and to the directors from time to time upon any loans exceeding one per cent of the paid-up capital of the bank which in their judgment are inadequately secured, but this provision shall not be construed to relieve any director from the due and proper discharge of the duties of a director."

This provision seems to go further than any other legislative enactment with regard to the duties of auditors. It is designed to broaden the responsibility of the auditor considerably beyond what is involved in certifying to the financial condition of the bank. It would seem that the auditors are

under no restriction as to the transactions or conditions on which they may report. Their report, under this section, must be transmitted or delivered by the auditors to the general manager at his office and to each director at his last known address, and it must be incorporated in the minutes of the next meeting of the directors.

Annual Report Important Duty

The work involved in preparing the annual report to the shareholders is, in the usual circumstances, the most important duty of the auditors. Their annual report must be addressed to the shareholders and submitted by the directors to the shareholders at their annual meeting. It is required that the report shall state:

- (a) whether or not they have obtained all the information and explanations they have required;
- (b) whether, in their opinion, the transactions of the bank which have come under their notice have been within the powers of the bank;
- (c) whether, in their opinion, the statement referred to in the report discloses the true condition of the bank;
- (d) whether the statement is as shown by the books of the bank.

Paragraphs (a), (c) and (d) are, for the most part, copied from the Companies Act which had been enacted by the Dominion and several of the provinces of Canada before these provisions were incorporated in the Bank Act. Paragraph (b), as to whether, in the opinion of the auditors, the transactions of the bank which have come under their notice have been within the powers of the bank, was original. This latter requirement placed a definite responsibility on the auditors to familiarize themselves with the powers given to banks by the Bank Act, and also the type of business which is prohibited by the Act.

The requirement that the auditors shall state whether, in their opinion, the statement referred to in the report discloses the true condition of the bank is, of course, the most impor-

tant. It involves the ascertainment by the auditor of the location and ownership of the assets, that all liabilities are disclosed and that all assets are valued on a fair basis or that adequate reserves have been established against them.

With regard to loans, elaborate files are maintained on all loans at the head office, and it is necessary for the auditor to examine these files, so as to satisfy himself as to the credit of the borrowers and to estimate what provision is necessary for losses. He must also, as stated above, classify loans as to current and non-current, as this information is called for in the report to shareholders.

Under current practice, it is not considered necessary to visit any of the branch offices other than a few of the more important ones. The reason for this is that each bank maintains an inspection department of its own, which makes frequent examinations of all branches. In addition, such loans as are carried locally are reported on periodically to the head office by the district inspectors, and, as stated, the head office maintains complete files regarding all loans. It will occur to you that, under such circumstances, collusion between two or more branches or between the head office and branches might make it possible to conceal a shortage from the auditors. Experience has shown, however, that this is a very unlikely occurrence. The only positive solution would be to examine cash and securities at the many hundreds of branches of each bank at the same time, which would be impossible from a practical viewpoint.

Auditor's Certificate Shown

The following is a typical certificate appearing on the annual statements of Canadian banks:

"To the Shareholders,

We have examined the above Statement of Liabilities and Assets at 30th November, 1932, with the books and accounts of
..... at Head Office and with the
certified returns from the branches. We have verified the cash and
securities at Head Office at the close of the Bank's fiscal year, and
during the year we counted the cash and examined the securities at
several of the important branches.

We have obtained all the information and explanations that we have required and, in our opinion, the transactions of the Bank which have come under our notice have been within the powers of the Bank. The above statement is, in our opinion, properly drawn up so as to disclose the true condition of the Bank as at 30th November, 1932, and it is as shown by the books of the Bank."

At this point it might be of interest to note the distinction between the duties of the auditors of a Canadian bank and of auditors engaged, say, by the examining committee of a New York state institution. In the latter, the responsibility for the examination is placed upon a committee of directors, and they are given power to employ such assistance as they may require. Thus, the usual practice, which has been developed, is that the accountants employed assume responsibility to the committee for verification of cash, exchanges, and securities, including notes receivable, bills receivable for loans and the collateral held in that connection, and also for the calculations of the market values of securities, but the committee themselves take full responsibility for the complete report including valuations of non-marketable securities and reserves against slow and doubtful loans. As will be noted from the explanations stated above, in Canada the auditors take full responsibility for all of these things, which, in New York State at least, they are not called upon to do.

The auditor's report must be attached to the statements submitted by the directors to the shareholders, and it has to be read before the shareholders in the annual general meeting. It is noted elsewhere that this report includes a very full statement of the financial condition of the bank.

If the shareholders require the directors to submit any statements of the affairs of the bank, other than the annual statement, the auditors must make a similar report on such statement, giving the same information, and that report must also be read to the shareholders at the next meeting and a copy mailed to every shareholder.

Penalties on Auditors

It is interesting to note that the penalty for issuing any false or deceptive statement is the same for the auditor as it is for any officer or director. Section 163 provides as follows:

"Every president, vice-president, director, auditor, general manager or other officer of the bank or trustee who *knowingly* prepares, signs, approves or concurs in any account, statement, return, report or document respecting the affairs of the bank containing any false or deceptive statement, or any return which does not set forth the true financial position of the bank including all the information required by section one hundred and thirteen of this Act, shall be guilty of an indictable offence punishable, unless a greater punishment is in any case by law prescribed therefor, by imprisonment for a term not exceeding five years."

Sub-section 2 provides a penalty of three years for a similar offense if done negligently as distinguished from knowingly.

You are, no doubt, interested to know whether any of the penalties for approving a false or deceptive statement, either knowingly or negligently, have ever been enforced. There is only one case on record — that of the Home Bank of Canada — which suspended payment on August 17, 1923. In that case, the auditor was found guilty of having negligently approved a statement contrary to the Bank Act, but he was not convicted of having done so wilfully.

In conclusion, is it not fair to say, in praise of the part which our professional brethren to the north of us have played in their banking situation, that the high regard on the part of the public for their work and the effect of the publication and circulation of their reports and certificates, has, in some measure at least, contributed not only to the excellent record of Canadian banks but also to the degree of confidence which their citizens recently displayed, in spite of the conditions which developed on this side of the border?

Is Specialization in the Practice of Accountancy a Desirable Development?

By MORRIS C. TROPER, C. P. A.,
of LOEB & TROPER

AT the Quarter Centennial of the Illinois Society of Certified Public Accountants held in Chicago in 1928, Mr. Ernest Reckitt in speaking on the subject of "Public Accounting in 1903" told the following story as a "rather funny incident indicating the attitude of the public in those days." He said, "I remember another fellow who wanted us to audit his books and I told him I would be very glad to do it. I thought I had him all nailed and that I had landed the job, but all of a sudden he said to me, 'Did you ever audit the books of a manufacturing concern that made mouse-traps?' From that point on I could see the case was lost, and even to this day I have never audited the books of a concern that manufactured mouse-traps."

The story was evidently told as a joke, and yet we are assembled here today to discuss seriously as part of our subject, the question as to whether that accountant should have lost an engagement because of his failure to specialize in a particular industry.

We are, and for sometime past have been, living in an era of specialization. This is an age in which we are getting to know more and more about less and less. Everything is specialized and it seems that everyone is seeking to become a specialist in something or another. In the trades, in business and in the professions, the first question is "What do they specialize in?"

We realize that it is difficult to compare one profession with another, and so no attempt will be made to draw comparisons with the legal, medical or other professions. While most of them have been highly specialized, unanimity of opinion on the subject has by no means prevailed, and some

of those who have been most ardent exponents of specialization are now beginning to lament over-specialization. Modern facilities in education and in practice have been developed to foster this trend, and specialization is only attempted, in most cases, after long years of general experience. Besides, a system has been built up wherein cases are usually referred to one another, and personal service to a very great extent characterizes their activities. In medicine, national examining boards have been established and the specialist must be recognized by those boards, and by general practitioners as well, in order to be considered as such. However, much confusion still exists and the public in general still considers it a hardship to have to go to a doctor to find out which doctor to go to, with the result that many aspersions are cast with regard to individual capabilities and fees.

Some Aspects of the Problem

The foregoing, in so far as it reflects on the practice of public accountancy, brings up questions of advanced educational and laboratory facilities in a situation where we do not have a single professional school which confines itself to certified public accountants; of personal service, where we are at present attempting to serve hundreds or thousands of clients, as the case may be; and of specializing, in a field the general aspects of which are still not entirely understood by those who come in contact with it.

Strange as it may seem, I have been able to find little, if any, material on this question in so far as it directly affects the practice of the public accountant, even after a fairly exhaustive search of library files and the indices of periodicals. While this eliminates the fear of contradiction based on authority, it makes it well nigh impossible to crystallize at any one time or in any one paper all that may be said on this subject. This start gives further evidence of the sturdy progressivism of your Society in discussing frankly and openly questions of general welfare, and should be an impetus to its members in attempting to envisage the developments of the future.

In the light of what has happened in the last few years I hesitate in making any prophecies whatsoever, but present trends in the practice of public accountancy have indicated some facts which represent one point of view and which demand our consideration.

We may well start with the experiences of any individual in almost any line of activity. The young man, when he first begins to think of his future is faced with a huge range of industrial, trade and professional pursuits, and must decide whether he is to enter some line of industry, learn a trade, or take up a profession. Having made his first decision he will then begin to think in a narrower sense of just what industry, trade or profession, he will elect to follow. Let us assume he decides to become a professional man and chooses engineering as his field. He next must give thought to the question as to which branch he desires to pursue—civil, electrical, chemical, or mechanical engineering. Later we find him concentrating on some particular subdivision of the work previously chosen, and possibly still later, on some subdivision of a subdivision—ad infinitum—as is so frequently the case in experimentation and research.

Human Endeavors Limited

What is the reason for the selective activities evidenced in all of these older professions? I believe you will find that in the last analysis, and leaving aside questions of aptitudes and personal likes and dislikes, it is ultimately due in the main to the physical limitation of time placed upon any person who attempts to acquire and use any part of the vast fund of knowledge which represents the sum total of human experiences thus far acquired. Eventually, the accountancy profession must go through the same development as that of the older professions. This seems inevitable and may come about much sooner than most of us anticipate.

As the young practitioner works his way up in our profession, it undoubtedly dawns upon him that there is much to be learned in special spheres of activity. He begins to ask himself whether he has done all the things he should do in a particular situation, and whether he knows all the things

he should know in order to permit him to do these things. He then starts to realize that if he were to apply this thought to all types of endeavor it would be physically impossible to acquire all the necessary knowledge and keep abreast of the times.

The scope of the accountant's horizon is ever receding. The limitation of today becomes the starting point of tomorrow, with the result that we are being carried into realms which at one time were thought to be quite beyond the province of our work. We practice a comparatively young profession; we question if any profession has ever had the meteoric rise that ours has experienced. If, figuratively speaking, we could train the highest powered telescope on the periphery of our activities, it would not be powerful enough to detail the enormous developments and opportunities that lie beyond. As these are realized, the necessity of restricting one's endeavors to just one sector of this unlimited field, must become more obvious.

Mr. M. V. Hayes in his book "Accounting for Executive Control" records the progress of accountancy in an ever widening scope from laying emphasis on the facts and accounts from the view point of proprietorship, to consideration of the interests of creditors and investors and finally through the assistance of cost, budget and other studies, to a valid recognition of the claim by business managers for information that will be of real value in the control of operations. Certified public accountants may develop here the type of service necessary to be of assistance to management, which may be made available to all business, large or small, and which may necessarily lead to specialization in types of services and even in certain major industries or trades.

The Future of Accounting

The theory is developed further in a paper by George E. Frazer, C. P. A., entitled "Public Accounting in 1953" and read at the Quarter Centennial previously mentioned. He made the following statements:

"The accountant of 1953 will write a report that would interest us today a great deal. He will start with an audit as

a diagnosis of business, but he won't stop there. He will start with the audit as the frame work—the preliminary thing that he as an accountant has to say. He will go on from the audit with a critical analysis of the economic factors of the business that produce the results recorded. He will not leave it to someone called management engineers, industrial engineers, God knows what, to attempt to interpret business conditions, but knowing that he stands soundly upon an audit of facts, soundly upon an analysis of the business he will present a critical analysis of how the balance sheet came about, and what the profit and loss statement records in terms of business movement during the period under review.

"They will not leave the budgets to be made by statisticians, business forecasters, and experimenters.

"As supplements to their reports the accountants will make cost analysis, systems, advice on tax matters; more than they do today because they will add to income taxation the growing problem of property taxation. Accountants will be asked to sit on government commissions and boards to represent economic interpretation.

"The accountant will sit on boards of directors to represent the thousands of stockholders who are not now represented in the ownership of the great corporations.

"I heartily believe that in 1953 the professional accountant will be the day by day adviser of the business that seeks his service. He will not be called in after the close of the year; he will be there throughout the year. Accounting in 1953 will be the most difficult profession in the world."

Services Will Be Specialized

I assume you will agree with me when I say that services such as these must necessarily be specialized. We undoubtedly have the beginnings of such activities in special types of service now being rendered such as cost data, budgets, special studies, investigations, tax work (which in itself may be specialized), opinions, etc., and in special industries or trades which require special technical knowledge, such as insurance, brokerage, estates, municipalities, etc.

Now, with the discussion of the future behind us, let us look at another point of view which confines itself to the situation as it exists today.

Our profession is still in its infancy. The practice of public accountancy did not become at all general in the United States until 1875 and the first C. P. A. Law, that of New York, was not passed until 1896. Today each of the 48 States, as well as Alaska, Hawaii, the Philippines, Porto Rico and the District of Columbia have a C. P. A. law, the last of which, I believe, was enacted as late as 1927. Besides, as you know only too well, the legal status of the practice in this State is still the subject of discussion and attempted legislation. From the functional standpoint, we are told by Professor Roy B. Kester of Columbia University that accounting in anything like a modern form is not of earlier origin than 1915.

Specialization is something that cannot be hurried; nor can it be forced. Constructive metamorphosis can only come about in a natural, orderly and timely way, as has happened in other professions. This process is going on now and will continue to go on.

Specialties Within Scope of C. P. A.

However, I believe, that today the activities of the rank and file of practitioners are confined generally and to a great extent to the auditing of books and records in the interest of the proprietor, the creditor or the potential investor, and that most of the special services required in local business are well within the possibilities of the certified public accountant of average experience.

A broad, general experience is, we believe, of value to every practitioner. As a matter of fact we know how eager our beginners are to seek employment where they can secure widely different kinds of work and we also know how desirable it becomes from time to time, to change men on various engagements because of the fact that they may become stale through an over amount of sameness. The term certified public accountant seems to indicate in its designation the fact that his services are for the public and may be called

upon to serve in a wide sphere of activities. It is in opposition to the narrowing influence of activity in some special trade, and I believe the average practitioner realizes the importance of a diversified practice.

The growth of the practice of an individual practitioner or of a firm may develop in one particular industry, but if it does and is confined to a great extent to little more than auditing services, I believe that it is fraught with some danger both to the client and to the practitioner. I would, however, hardly call this professional specialization in the true sense of the word. A more appropriate term to be applied is really standardization, and this, in itself, ought to give no more assurance of calibre of service than might be expected from the average practitioner. As a matter of fact, the opposite might easily be true because of the more varied experience of the latter.

I believe it is true also that where we find standardization of this type there is no attempt within the organization to refrain from doing work of other types even though such work may be in an entirely different trade or industry. In other words, while such practitioners desire to be called specialists in one line, there is no hesitancy whatsoever in accepting engagements in other lines.

Circumstances Lead To Specialization

Of course such a condition can very easily be brought about where the individual practitioner or firm starts in business, secures an engagement in a certain trade or industry, and then gradually confines his or their efforts to securing business in that industry alone. Business may, as a matter of fact, come more easily that way. Success in one or more engagements in a particular trade may bring others—and this in spite of the fact that the initial success may have been due not to any particular knowledge on the part of the practitioner in the particular trade but to his broad general training. But I reiterate that the individual who builds up this kind of a practice is doing himself, from a professional standpoint, more harm than good. I wonder if this sameness

of work along one line will not ultimately cause him to see the trees instead of the forest and whether the generally experienced practitioner will not accomplish at least the same results without exposing himself to the dangers involved in this so-called specialization.

The development and growth of trade and credit organizations have undoubtedly had a decided influence in expansion along these lines and as a means toward these ends. While such a procedure in building a clientele may be lucrative to the individual, the question arises as to whether it is of benefit to the profession as a whole, especially where attempts are made to increase this practice to the detriment of other practitioners on the basis of specialization. As a matter of fact, frequent rumors are heard that this type of specialist has been, and is being, created by the confidence or even favoritism which certain individuals or groups of individuals in the business world show towards him.

This situation when encountered is, to say the least, unfair, and recognition of such specialization from within the profession is, of course, out of the question. In so far as favoritism on a wholesale scale is concerned, I believe it is fast disappearing in all serious-minded business. Confidence, on the other hand, is a problem of the profession as a whole. The general public and surely those who come into immediate contact with us must be taught to realize generically what the term certified public accountant means so that when names are mentioned it will be absurd to pass them off with the comment "We do not know him or them," as the case may be. The fact that he is a certified public accountant should gradually be brought to instill the same confidence in the ordinary situation as known names. However, suffice it to say that the practices of this group are fraught with much danger for they can be broken down in the same manner as they are made, only often times much faster. But even this does not do much good to certified public accountants as a class.

On the other hand we should not be too prone to criticize this desire for personal confidence where it is honestly made,

even where it directly affects us. We must realize that those who have financial risks feel entitled to what they term "a feeling of protection" as well as actual protection and we must reconcile ourselves to this situation until such time as we can by educational processes give assurance that such confidence may be placed in the great rank and file of practitioners. The greater our numbers become, the more acute becomes the problem. It will take time to achieve this end but I believe that concerted action will quicken its accomplishment.

Young Accountants and Their Problems

Unfortunately, some members of our profession, because of immaturity, insufficient compensation, or for other reasons, have been forced into situations which have not always redounded to their credit, but a lack of experience on the part of some should not be used as an argument for so-called specialization by others. Besides, I do not believe that it is presumptuous to state that most young accountants have learned that their education is not complete upon the passing of an examination or even after they have had sufficient experience to develop some ability to use sound judgment. In addition, a far greater degree of wisdom must be acquired through careful study of new methods and constant vigilance in attempting to improve existing systems. The time has passed when we can hope to impress business men with methods which have nothing to recommend them except mere adherence to traditional forms and practice. Development along these lines will go a long way in assisting the general practitioner in retaining his legitimate sphere of activity, and in disillusioning the much overworked term of specialization when none actually exists, and where, further, none is actually required. While there may be a legitimate sphere for specialization in types of service such as cost accounting, tax work, special trades, or work performed in the assistance of managerial administration, it is hard to be convinced that the primary functions of the public accountant should now be specialized for each and every trade. If we go back to our old text books I believe we will find but a

small fractional part thereof devoted to what was called "special audits". These dwelt mostly on some different procedures in different types of business, but none was beyond the scope of the average experienced practitioner.

I recollect being asked by a client to investigate the affairs of a company which manufactured a grape drink in order to ascertain whether or not he should invest some \$50,000 in the proposition. My knowledge of that particular industry was no more and possibly less than that of the average lay person. However, after but a brief survey I was convinced that my client should not risk his money. Although someone else did invest, the firm was in bankruptcy within three months. A fellow-accountant tells me he was called in for the first time to audit the accounts of a subway construction company. He feels he did a fine piece of work and obviates any thought of conceit by immediately stating that in his opinion any experienced accountant could have done the same. It needed no specialist.

On the other hand, I know of a case where accountants who had confined themselves to a certain line of industry, had been engaged by a concern in that industry for a period of over ten years. This would indicate that the results of their work had been satisfactory not only to their employers but also to the numerous credit grantors who had been extending credit. Yet, when this concern found itself in an embarrassed condition certain creditors felt that it would be the part of wisdom to employ other accountants. This was done and the report rendered by these accountants brought in so many new phases of the conditions which had led up to the embarrassment that the creditors were amazed that the so-called specialist had not been aware of them. These experiences can be multiplied, undoubtedly, by the experiences of each and every one of you.

This has led me, as a matter of interest, to glance through some of our own accounts and, without attempting any particular arrangement, I find that from time to time we have performed services including auditing, systematizing, budget-

ing, cost studies, tax work, etc. for about seventy-five and more groups.

Specialization Considered Unnecessary

I am sure that this partial total can be added to by many of you. Some may say that from a business getting standpoint and even from the standpoint of professional capability, we should have confined ourselves to some particular industry, or to related industries, or at least to some few of these industries. However, the vast majority of accountants, whose experiences along these lines I have sought, feel that such specialization is basically unnecessary from every standpoint, and even harmful. My feeling is that the certified public accountant with a fair amount of general experience will deliver the goods every time. His first engagement may possibly be less profitable to him than to someone who finds himself at home in the situation, but he will do it, even at a loss—if you will—and it will be done well.

I must admit that with the disrupted conditions existing in business today, with no new enterprises being formed, with the certified public accountant being the first to go in an effort to reduce overhead, with commercial credit being granted on the basis of calculating the amount of the settlement in advance, and with banking credit reduced to a matter of saying "no" in the most polite manner, the subject may become academic for many practitioners. They will take as many engagements in one industry or in as many industries as they may be fortunate enough to get. But perhaps this is beside the point!

It is impossible, in a paper of this size, to run the subject ragged, or even to reach such conclusions as will stand the tribulations of every day practice, or the test of changing times. Besides, paramount issues always live on. All that can be hoped for is to provoke sufficient thought and interest to the end that it will tend towards constructive and well considered discussion.

With a full recognition of the homely virtues of the work performed by those pioneers who have gone before us, we must, in the same spirit, foster safe and sane developments for those who are to carry on the torch from the point where we leave off; and this can only be accomplished through unanimity of interest in the general welfare of the profession on the part of all of us.

In closing, I ask you—should Mr. Reckitt have lost the mouse-trap audit?

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Objects of the Society

"To cultivate, promote and disseminate knowledge and information concerning accountancy and subjects related thereto; to establish and maintain high standards of integrity, honor and character among certified public accountants; to furnish information regarding accountancy and the practice and methods thereof to its members, and to other persons interested therein, and to the general public; to protect the interests of its members and of the general public with respect to the practice of accountancy; to promote reforms in the law; to provide lectures, and to cause the publication of articles, relating to accountancy and the practice and methods thereof; to correspond and hold relations with other organizations of accountants, both within and without the United States of America; to establish and maintain a library, and reading rooms, meeting rooms and social rooms for the use of its members; to promote social intercourse among its own members and between its own members and the members of other organizations of accountants and other persons interested in accountancy or related subjects; and to do any and all things which shall be lawful and appropriate in furtherance of any of the purposes hereinbefore expressed."

—From the Certificate of Incorporation.